

Before the  
**FEDERAL COMMUNICATIONS COMMISSION**  
 Washington, D.C. 20554

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**Federal Communications Commission  
Office of Secretary**

**In the Matter of**

## Forbearance From Depreciation Regulation of Price Cap Local Exchange Carriers

96-198

**PETITION FOR FORBEARANCE**  
**OF THE**  
**UNITED STATES TELEPHONE ASSOCIATION**

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## SUMMARY

USTA hereby petitions the Commission to forbear, as of January 1, 1999, from regulating the depreciation and amortization practices of local exchange carriers subject to price cap regulation. USTA specifically requests the Commission to forbear from enforcing sections 32.2000(g) and (h) and 43.43 of the Commission's rules, which address depreciation accounting and reporting, and from conducting depreciation prescription proceedings pursuant to section 220(b) of the Communications Act.

The requested forbearance is long overdue with respect to the price cap LECs. The Telecommunications Act of 1996 amended section 220(b) so that the Commission no longer is required to prescribe or otherwise regulate depreciation rates. In 1997, the Commission eliminated the sharing mechanism formerly imposed on price cap LECs. Safeguarding that mechanism had been a major reason for retaining depreciation regulation of these LECs.

As this petition shows, forbearance from depreciation regulation of the price cap LECs is required under section 10 of the Communications Act. The three factors listed in section 10 mandate such forbearance.

First, depreciation regulation of price cap LECs is not necessary to ensure that their charges, practices, classifications, regulations, or other activities are just and reasonable and are not unjustly or unreasonably discriminatory. Under price cap regulation, any link between depreciation prescriptions and a LEC's charges or other activities is extremely attenuated.

Second, such regulation is not needed to protect consumers. To the contrary, continued depreciation regulation harms consumers by imposing unnecessary administrative burdens and costs on price cap LECs and the Commission.

Third, forbearance from depreciation regulation is in the public interest. In addition to the benefits described above, forbearance would promote competition by improving the efficiency of the price cap LECs' operations. Unnecessary regulation, such as depreciation regulation of price cap LECs, is contrary to the public interest because it burdens these LECs relative to their unregulated competitors. Forbearance will also serve the public interest by permitting the Commission to deploy its resources in areas that more directly implement the competitive goals of the 1996 Act.

In addition to section 10, forbearance from depreciation regulation of price cap LECs is consistent with section 11 of the Communications Act. Section 11 charges the Commission, as part of its biennial review of regulation, to repeal or modify any regulation determined not to be in the public interest as the result of meaningful economic competition between providers of such service. Because price cap regulation effectively replicates the competitive process without relying on the depreciation rules now in effect, such rules are unnecessary and contrary to the public interest. With respect to depreciation regulation, forbearance is an appropriate means of satisfying section 11.

USTA requests the Commission to address this petition expeditiously, so that forbearance from depreciation regulation of price cap LECs can take effect on January 1, 1999. Rapid action will help consumers of the services provided by price cap LECs by promoting rational, market-based infrastructure development.

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**PETITION FOR FORBEARANCE OF THE  
UNITED STATES TELEPHONE ASSOCIATION**

**I. INTRODUCTION AND OVERVIEW**

The United States Telephone Association ("USTA") hereby petitions the Commission to forbear, as of January 1, 1999, from regulating the depreciation and amortization practices ("depreciation regulation") of local exchange carriers subject to price cap regulation ("price cap LECs").<sup>1/</sup> USTA specifically asks the Commission to forbear from enforcing sections 32.2000(g) and (h) and 43.43 of the Commission's rules, which address depreciation accounting and reporting, and from conducting depreciation prescription proceedings pursuant to section 220(b) of the Communications Act.<sup>2/</sup> Such forbearance is a long-overdue reform of the Commission's regulation of the price cap LECs, especially in light of

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<sup>1/</sup> This petition is filed pursuant to section 10(c) of the Communications Act of 1934, as amended (the "Communications Act"), 47 U.S.C. § 160(c). USTA, an association whose members are LECs, fulfills the statutory definition of a "class of telecommunications carriers."

<sup>2/</sup> See 47 C.F.R. §§ 32.2000(g), (h), 43.43; 47 U.S.C. § 220(b).

the Commission's elimination in 1997 of the so-called "sharing" mechanism formerly imposed on those LECs. The requested forbearance is required under section 10 of the Communications Act,<sup>3/</sup> and is consistent with the Commission's biennial review of regulations now taking place pursuant to section 11 of the Communications Act.<sup>4/</sup>

The three factors of section 10 mandate forbearance from depreciation regulation of price cap LECs. First, depreciation regulation of price cap LECs is not necessary to ensure that their charges or other activities are just and reasonable and are not unjustly or unreasonably discriminatory. Second, such regulation is not needed to protect consumers. To the contrary, continued depreciation regulation harms consumers by imposing unnecessary administrative burdens and costs on price cap LECs and the Commission.

Third, forbearance from depreciation regulation is in the public interest. In addition to the benefits described above, forbearance would promote competition by improving the efficiency of the price cap LECs' operations. Unnecessary regulation, such as depreciation regulation of price cap LECs, is contrary to the public interest because it burdens its subject firms -- price cap LECs -- relative to their unregulated competitors. Forbearance will also serve the public interest by permitting the Commission to deploy its resources in areas that more directly implement the competitive goals of the 1996 Act.<sup>5/</sup>

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<sup>3/</sup> See *id.* § 160.

<sup>4/</sup> See *id.* § 161. As part of the 1998 biennial review, Arthur Andersen LLP recently filed with the Commission a position paper recommending that price cap LECs should be relieved of "the costs associated with the depreciation represervation process" and should be allowed to implement depreciation practices consistent with generally accepted accounting principles ("GAAP"). See Arthur Andersen LLP, *Accounting Simplification In The Telecommunication Industry*, *ex parte* filing in General Action, Report No. GN 98-1, CC Docket No. 98-81, ASD File 98-64 (filed July 15, 1998) at 30.

<sup>5/</sup> When forbearance takes effect, individual price cap LECs should not be precluded from making their cases to recover any depreciation reserve deficiencies that may exist.

In addition to section 10, section 11 of the Communications Act charges the Commission, as part of its biennial review of regulation, to "repeal or modify" any regulation determined not to be in the public interest "as the result of meaningful economic competition between providers of such service."<sup>6/</sup> Because price cap regulation effectively replicates the competitive process without relying on the depreciation rules now in effect, such rules are unnecessary and contrary to the public interest. Forbearance is an appropriate means of addressing such regulation consistent with section 11.<sup>7/</sup>

## II. THE LEGAL AND POLICY REASONS FOR DEPRECIATION REGULATION OF PRICE CAP LECS NO LONGER EXIST

Prior to passage of the Telecommunications Act of 1996 (the "1996 Act"), section 220(b) of the Communications Act required the Commission to prescribe depreciation rates

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<sup>6/</sup> See *id.* § 161(b).

<sup>7/</sup> USTA notes that the Commission has sought proposals for "accounts or filing requirements that could be reduced or eliminated." See *1998 Biennial Regulatory Review -- Review of Accounting and Cost Allocation Requirements; United States Telephone Association Petition for Rulemaking*, CC Docket No. 98-81, ASD File No. 98-64, Notice of Proposed Rulemaking, FCC 98-108 (rel. June 17, 1998).

for common carriers.<sup>8/</sup> Recognizing the need for depreciation reform as the telecommunications marketplace changes, the 1996 Act amended section 220(b):

The Commission *may* prescribe *for such carriers as it determines to be appropriate*, the classes of property for which depreciation charges may properly be included under operating expenses, and the percentages of depreciation which shall be charged with respect to each of such classes of property, classifying the carriers as it may deem proper for this purpose. The Commission may, when it deems necessary, modify the classes and percentages so prescribed....<sup>9/</sup>

Due to that amendment, the Commission no longer is required to prescribe or otherwise regulate depreciation rates. In drafting the 1996 Act, the Conference Committee adopted the Senate's treatment of this issue. As the Joint Explanatory Statement noted:

[The amendment] repeals the current requirement that the Commission set depreciation rates for common carriers, thus allowing the Commission flexibility to assess whether doing so would serve the public interest.<sup>10/</sup>

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<sup>8/</sup> For the text of the former version of section 220(b), *see* 47 U.S.C. § 220(b) (1995):

The Commission shall prescribe for such [common] carriers the classes of property for which depreciation charges may be properly included under operating expenses, and the percentages of depreciation which shall be charged with respect to each of such classes of property, classifying the carriers as it may deem proper for this purpose. The Commission may, when it deems necessary, modify the classes and percentages so prescribed....

The Commission has authority over carriers' interstate depreciation practices, while the states have authority over intrastate depreciation.

<sup>9/</sup> *Id.* § 220(b)(1996) (emphasis added).

<sup>10/</sup> Joint Explanatory Statement of the Committee of Conference, *printed in* H.R. Conf. Rep. No. 104-58 (Jan. 31, 1996) at 186.



Despite this statutory change, the Commission's regulations regarding depreciation and amortization, including sections 32.2000(g) and (h) and 43.43, continue to apply as they did before passage of the 1996 Act.

Current depreciation rules for price cap LECs are artifacts of rate-of-return regulation. In the price cap context, these rules were used to control potential manipulation of costs, in order to safeguard the sharing mechanism previously in place for price cap regulation. That mechanism depended in part on the level of a LEC's reported earnings, which were calculated on the basis of rate-of-return regulatory methods.<sup>11/</sup> This major reason for retaining depreciation regulation ended in 1997, when the Commission eliminated the sharing mechanism for all price cap LECs.<sup>12/</sup>

However, the depreciation rules remain in operation. Section 32.2000(g) of the Commission's rules prescribes depreciation accounting practices for all LECs.<sup>13/</sup> Under these provisions, all LECs must calculate depreciation rates using a so-called "group plan of accounting for depreciation."<sup>14/</sup> The Commission only permits the use of straight-line

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<sup>11/</sup> See *Simplification of the Depreciation Prescription Process*, 8 FCC Rcd 8025 (1993) ("Depreciation Simplification Order") ¶¶ 20 n. 28, 27. The Commission's interim price cap plan permitted LECs to choose among three "X-factors," or productivity adjustments, two of which included sharing mechanisms. Under these sharing mechanisms, price cap LECs were required to "share" half or all earnings above specified rates of return with their access customers by lowering the maximum rates that the LECs could charge during the next year. See *Price Cap Performance Review for Local Exchange Carriers; Access Charge Reform*, 12 FCC Rcd 16642 (1997) (the "Price Cap Order") ¶ 10.

<sup>12/</sup> See *id.* ¶ 11.

<sup>13/</sup> Section 32.2000(h), from which USTA also seeks forbearance, requires straight-line methods of amortization as well.

<sup>14/</sup> See 47 C.F.R. § 32.2000(g).

depreciation,<sup>15/</sup> although at different times it has allowed the use of several different straight-line methods.<sup>16/</sup>

Under the current rules, the Commission must approve each LEC's depreciation rates for the various types of plant used in providing interstate services. This prescription process traditionally has occurred roughly every three years. While the Commission attempted to simplify its depreciation prescription procedures in 1993,<sup>17/</sup> the changes it adopted did not relieve LECs of preparing voluminous and detailed studies if they seek depreciation rates outside of prescribed ranges. Section 43.43 of the Commission's rules details the reporting and data requirements that LECs must satisfy when seeking to change these rates.

The Commission's processes for regulating depreciation historically have been controversial and labor-intensive, and have consumed significant resources from the Commission staff as well as the regulated LECs.<sup>18/</sup> Under rate-of-return regulation, depreciation regulation has been used as a tool for limiting the LECs' apparent costs of service by adopting long asset lives in order to reduce depreciation rates. Doing so lowered

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<sup>15/</sup> See *id.* §§ 32.2000(g)(1)(i), (2)(i).

<sup>16/</sup> These methods include straight-line remaining-life, equal life group, and whole life depreciation.

<sup>17/</sup> See Depreciation Simplification Order; *Simplification of the Depreciation Prescription Process*, Second Report and Order, 9 FCC Rcd 3206 (1994) ("Second Simplification Order"). The Commission permitted carriers to make streamlined filings for changes in depreciation rates if their underlying factors fall within prescribed ranges.

<sup>18/</sup> See, e.g., *Amendment of Part 31 (Uniform System of Accounts for Class A and Class B Telephone Companies)*, 83 FCC 2d 267 (1980), *recon.* 87 FCC 2d 916 (1981), *Supplemental Opinion and Order*, 87 FCC 2d 1112 (1981), *aff'd sub nom. Southern Bell Telephone and Telegraph Company v. FCC*, No. 84-1638 (D.C. Cir. Jan. 17, 1986); *The Prescription of Revised Percentages of Depreciation Pursuant to the Communications Act of 1934, as Amended, for: General Telephone Company of Florida, et al.*, 3 FCC Rcd 1216; (1988), *erratum* (rel. Feb. 19, 1988); Depreciation Simplification Order, *supra*; *Order Inviting Comment* (rel. Nov. 12, 1993), Second Simplification Order, *supra*.

the LECs' ostensible costs of service for regulatory purposes, which under rate-of-return regulation translated to decreased rates.<sup>19/</sup>

The Commission's present form of price cap regulation for LECs is designed to replicate the beneficial incentives of competition on LEC interstate access services, while reasonably balancing the interests of ratepayers and LEC stockholders.<sup>20/</sup> As the Commission has explained:

Rather than adjusting prices to allow LECs the opportunity to earn a pre-determined return on interstate investment, price cap regulation directly regulates prices and allows earnings to vary. Under price cap regulation, the ceiling or maximum price a LEC can charge for interstate access is adjusted annually by a measure of inflation minus an "X-factor." A separate adjustment is made for "exogenous" cost changes, which are changes outside the carrier's control and not otherwise reflected in the price cap formula.<sup>21/</sup>

In 1993, after the imposition of price cap regulation on LECs, the Commission decided to adopt its current depreciation reporting requirements in large part to preserve the sharing mechanism. As noted above, however, the Commission eliminated the sharing mechanism in 1997.

As a result, the Commission's principal rationale for its existing depreciation practices no longer applies -- especially in light of the flexible treatment of depreciation regulation authorized by the 1996 Act. With the removal of the sharing mechanism, depreciation regulation is not only unnecessary for price cap regulation, it is counterproductive because it continues to impose costs on price cap LECs and the Commission alike. Indeed, the Price

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<sup>19/</sup> It is questionable in today's telecommunications marketplace whether current interstate depreciation practices are effective for LECs subject to rate-of-return regulation.

<sup>20/</sup> See Price Cap Order ¶ 2.

<sup>21/</sup> *Id.* ¶ 3.

Cap Order raised the prospect of depreciation reform before the next performance review. Although the Price Cap Order used previously prescribed depreciation rates in calculating Total Factor Productivity ("TFP") for purposes of determining the X-factor in the current price cap plan,<sup>22/</sup> the Commission characterized its decision to do so as "limited findings" regarding depreciation, and held out the possibility of discontinuing depreciation regulation:

Nor are we suggesting that we plan to continue exercising our Section 220(b) prescription authority indefinitely. The 1996 Act amended Section 220(b) of the Communications Act, so that we are no longer required to prescribe depreciation rates. The telecommunications industry is evolving, and this evolution may well require us to revise our prescription methods, or possibly discontinue depreciation rate prescriptions altogether.<sup>23/</sup>

This reasoning strongly supports immediate forbearance. In the face of rapid technological change and competition, spurred by the 1996 Act, depreciation regulation of price cap LECs is not needed to serve the interests of consumers. Regulated depreciation, by its nature, is economically unsound. For example, when innovation occurs rapidly, as is the case in the telecommunications industry, an asset's economic life generally is shorter than its "useful life" prescribed under regulation.<sup>24/</sup>

In light of these developments, forbearance from depreciation regulation of price cap LECs is required under section 10 of the Communications Act. Forbearance, rather than yet

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<sup>22/</sup> See *id.* ¶ 65.

<sup>23/</sup> *Id.*

<sup>24/</sup> As USTA has explained in other proceedings, the Commission's depreciation prescriptions rely on, among other things, LEC net salvage rates, retirements, and remaining lives, rather than the economic obsolescence of capital. See USTA Comments in CC Docket No. 94-1, 96-262 (filed Jan. 16, 1996) at 18-19; USTA Reply in CC Docket No. 94-1, 96-262 (filed Mar. 1, 1996), Att. D at 2-6.

another rulemaking on depreciation regulation, is the most reasonable Commission response to the present situation.

The public interest would not be served by further attempts to retain or adjust interstate depreciation regulation for price cap LECs. A rulemaking on depreciation regulation would not supplant the statutory mandate to forbear from regulation when the provisions of section 10 are satisfied. Pursuant to section 10(a), the Commission must forbear from depreciation regulation of price cap LECs if:

- (1) enforcement of such regulation or provision is not necessary to ensure that the charges, practices, classifications, or regulations by, for, or in connection with that telecommunications carrier or telecommunications service are just and reasonable and are not unjustly or unreasonably discriminatory;
- (2) enforcement of such regulation or provision is not necessary for the protection of consumers; and
- (3) forbearance from applying such provision or regulation is consistent with the public interest.<sup>25/</sup>

In making the public interest determination required by section 10(a)(3), the Commission must consider whether forbearance "will promote competitive market conditions, including the extent to which such forbearance will enhance competition among providers of telecommunications services."<sup>26/</sup> If the Commission determines that such forbearance will promote competition among providers of telecommunications services, that determination "may be" the basis for an FCC finding that forbearance is in the public interest.<sup>27/</sup>

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<sup>25/</sup> See 47 U.S.C. § 160(a)(1)-(3).

<sup>26/</sup> See section 10(b) of the Communications Act, 47 U.S.C. § 160(b).

<sup>27/</sup> See *id.*

Because forbearance from depreciation regulation of price cap LECs meets these criteria, section 10 of the Communications Act requires forbearance from such regulation.

### III. FORBEARANCE FROM DEPRECIATION REGULATION OF PRICE CAP LECs IS REQUIRED UNDER THE COMMUNICATIONS ACT

#### A. Depreciation Regulation Is Not Necessary To Ensure That Price Cap LECs' Charges, Practices, Classifications, Regulations, Or Other Activities Are Just And Reasonable And Are Not Unjustly Or Unreasonably Discriminatory

With respect to section 10(a)(1) of the Communications Act, depreciation regulation of price cap LECs is not needed to ensure that the charges, practices, classifications, or regulations by, for, or in connection with these LECs are just and reasonable. Under the Commission's current price cap plan, LEC prices for interstate access service no longer directly depend on their costs of service derived through regulation. Access prices are limited by caps that, in turn, are determined under the price cap formula. That formula relies on economic indicators and exogenous adjustments, not LEC costs of service.<sup>28/</sup>

Ongoing regulation of the depreciation practices of price cap LECs is unrelated to assuring that the LECs' charges, or any other practices, classifications, or regulations, are

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<sup>28/</sup> Indeed, when contemplating depreciation reform in the Price Cap Order, the Commission stated that:

If we do revise the price cap LECs' depreciation rates, or if we permit them to develop their own depreciation rates, we will determine the effect of the revised depreciation rates on TFP and the X-Factor in our next performance review.

just and reasonable.<sup>29/</sup> As noted above, in prior Commission analyses, a major reason for retaining depreciation regulation was to preserve the operation of the price cap sharing mechanism. That mechanism relied on regulated earning levels, which in turn reflected depreciation prescriptions.<sup>30/</sup> With the Price Cap Order's elimination of the sharing mechanism, this justification for depreciation regulation no longer exists.<sup>31/</sup>

Nor is the Commission planning to rely on depreciation regulation in its next performance review of price cap regulation, scheduled to begin in 1999. The Commission is focusing on directly evaluating TFP and the X-factor rather than reported earnings, which depend on depreciation prescriptions:

[W]e would plan to make adjustments [in the next performance review] based on demonstrated industry-wide performance or other generic factors, rather than adjustments that are tied to a particular price cap incumbent LEC's interstate earnings.<sup>32/</sup>

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<sup>29/</sup> Commission forbearance from depreciation regulation of price cap LECs will not affect the authority of state regulators over the intrastate operations of those LECs. States that continue to rely on cost-of-service methods, including depreciation calculations, for intrastate regulation, retain the ability to examine depreciation rates independently of Commission action.

<sup>30/</sup> See Depreciation Simplification Order ¶¶ 20 n. 28, 27.

<sup>31/</sup> With regard to the possibility of misallocation of costs, the Commission has recognized that

The removal of sharing also removes a major vestige of rate-of-return regulation that created incentives to shift costs between services to evade sharing in the interstate jurisdiction.

See Price Cap Order ¶ 148.

<sup>32/</sup> See *id.* ¶ 167.

This again indicates that depreciation regulation is unnecessary to ensure that charges are just and reasonable.

The only remaining link between reported costs and prices in interstate price cap regulation is the low-end adjustment mechanism, under which a LEC may make a one-time upward adjustment to its price cap indices if its reported rate of return falls below 10.25%.

The low-end adjustment is rarely triggered. As a result, any link between depreciation prescriptions and charges under price cap regulation is extremely attenuated. However, if a price cap LEC seeks to implement a low end adjustment after forbearance takes effect, USTA recommends that the LEC should be responsible for demonstrating, at the Commission staff's request, that the LEC's depreciation practices are reasonable and did not distort the LEC's reported earnings.<sup>33/</sup>

Depreciation regulation is not otherwise necessary to ensure that charges, practices, classifications, or regulations by, for, or in connection with price cap LECs are just and reasonable. Indeed, the parameters derived from Commission depreciation regulation do not necessarily reflect economic realities. As such they are of limited analytic use to federal or state regulators, particularly as competition develops.<sup>34/</sup>

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<sup>33/</sup> The Commission has asked for comment on the possibility that changes to the separations rules could affect the level of prices paid by consumers, noting that the low-end adjustment maintains a link between costs and prices "under limited circumstances." See *Jurisdictional Separations Reform and Referral to the Federal-State Joint Board*, Notice of Proposed Rulemaking, 12 FCC Rcd 22120 (1997) ¶¶ 29, 85 n. 148. Because of the very limited use of the low-end adjustment, forbearance from depreciation regulation of price cap LECs would not have an appreciable effect on such price levels.

<sup>34/</sup> Those state commissions that continue to use cost-of-service regulation for intrastate purposes retain the ability to use independently available information to evaluate and apply depreciation rates.



As part of publicly-held and traded corporations, price cap LECs are subject to a myriad of financial and accounting rules and safeguards that ensure that their practices are comparable with those of other similarly-situated companies. Securities and Exchange Commission ("SEC") regulations, stock exchange listing requirements, audit oversight by independent public accountants, internal audits to assess internal controls, and compliance with generally accepted accounting principles ("GAAP") are examples of such safeguards.

Depreciation regulation is not necessary to ensure that price cap LECs' charges or other activities are not unjustly or unreasonably discriminatory. Depreciation regulation plays virtually no role in policing discrimination, especially in the case of price cap LECs. Forbearance from such regulation would provide no opportunity for price cap LECs to discriminate among or against any of their competitors or customers.

Completely separate from depreciation regulation, the Communications Act and the Commission's rules provide numerous safeguards against discrimination by telecommunications carriers, including sections 251 (interconnection), 254 (universal service) 255 (access by persons with disabilities), 256 (coordination for interconnectivity), 258 (illegal changes in subscriber carrier selections) 259 (infrastructure sharing), and 260 (telemessaging) of the Communications Act, and the Commission's regulations thereunder.<sup>35/</sup>

In addition, the full panoply of the Commission's enforcement mechanisms remains in effect under section 208 of the Communications Act to ensure that charges, practices, classifications, and regulations of price cap LECs are just and reasonable and are not unjustly or unreasonably discriminatory.<sup>36/</sup>

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<sup>35/</sup> See 47 U.S.C. §§ 251, 254, 255, 256, 258, 259, and 260.

<sup>36/</sup> See 47 U.S.C. § 208.

Competition disciplines the "charges, practices, classifications, and regulations" of price cap LECs more effectively than any indirect and attenuated effects of depreciation regulation. The growth among competitive access providers ("CAPs") and competitive local exchange carriers ("CLECs")<sup>37/</sup> means that competition in the provision of interstate access services is an increasingly effective way of ensuring that price cap LECs' charges and other activities are just and reasonable and are not unjustly or unreasonably discriminatory.

**B. Depreciation Regulation Of Price Cap LECs Is Unnecessary To Protect Consumers**

Regarding section 10(a)(2) of the Communications Act, the Commission's existing price cap regulations, tariffing requirements, enforcement mechanisms, and increasing competition are more than sufficient to protect consumers, independent of depreciation regulation. Depreciation regulation is not needed to protect the consumers of price cap LECs' interstate services.<sup>38/</sup>

As demonstrated above, forbearance from depreciation regulation will not have a significant effect on the comprehensive price cap regulation now imposed on LECs, a major

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<sup>37/</sup> See, e.g., *Merged AT&T-Teleport Offers New Services*, Comm. Daily (Mon. Jul. 27, 1998) at 1-2.

<sup>38/</sup> Indeed, satisfaction of section 10(a)(1) of Communications Act, as demonstrated above, is a strong indication that the regulation at issue is not necessary for consumer protection. See *Bell Operating Companies; Petitions for Forbearance from the Application of Section 272 of the Communications Act, As Amended, to Certain Activities*, (Com. Car. Bur. rel. Feb. 6, 1998) ("Section 272 Forbearance Order") ¶ 44; *Policy and Rules Concerning the Interstate, Interexchange Marketplace, Implementation of Section 254(g) of the Communications Act of 1934, as amended*, 11 FCC Rcd 20730 (1996) ("Interexchange Forbearance Order") ¶ 36. The Interexchange Forbearance Order was stayed by the D.C. Circuit on other grounds in *MCI Telecommunications Corp. v FCC*, No. 96-2459 (D.C. Cir. Feb. 13, 1997), but the Commission substantially affirmed it on reconsideration. See *Order on Reconsideration*, 12 FCC Rcd 15015 (1997).

goal of which is to protect consumers. Price cap LECs' charges for interstate services would continue to be subject to the Commission's active oversight pursuant to price cap regulation. With the elimination of the sharing mechanism, the principal link between price cap regulation and depreciation has already been severed,<sup>39/</sup> with no harm to U.S. consumers. Forbearance from depreciation regulation of price cap LECs accordingly would not decrease any protections that consumers now have due to price cap regulation.

Under the Commission's current tariffing requirements and reporting obligations, price cap LECs provide detailed and comprehensive information about their charges, terms, and conditions for interstate service, including voluminous supporting data.<sup>40/</sup> This information is readily available to consumers as well as Commission staff to use in assessing, and, if necessary, challenging the lawfulness of such carriers' rates, practices, and classifications. In this regard, the Commission's enforcement processes remain in effect under section 208 of the Communications Act as a prime means of protecting consumers by ensuring that charges, practices, classifications, and regulations of price cap LECs are just and reasonable and are not unjustly or unreasonably discriminatory.

In addition to the Commission's consumer protection apparatus, numerous safeguards are in place that will continue to protect consumers' interests. State regulation of the intrastate aspects of price cap LECs' operations will continue. Moreover, continued compliance by the price cap LECs with the financial and accounting requirements discussed

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<sup>39/</sup> As noted above, the low-end adjustment mechanism for price cap LECs maintains only a very attenuated connection between the price cap plan and depreciation.

<sup>40/</sup> See, e.g., 47 C.F.R. §§ 43.21 (reporting requirements) 61.42-61.49 (tariffing requirements). See also *1998 Biennial Regulatory Review -- Review of ARMIS Reporting Requirements*, CC Docket No. 98-117, Notice of Proposed Rulemaking, FCC 98-147 (rel. Jul. 17, 1998).

above -- including SEC regulations, stock exchange listing requirements, audit requirements, and GAAP -- provides additional assurances, that consumers will be protected in the absence of depreciation regulation.

As telecommunications competition grows, it protects consumers more effectively than depreciation regulation ever could or will. Competition give consumers choices among service providers and options that afford them opportunities to select the services that best fit their particular needs. At the same time, a competitive marketplace provides competitors with every incentive to report or publicize behavior by their rivals that is even arguably against consumers' interests. Forbearance from depreciation regulation does not alter these incentives that help protect consumers.

**C. Forbearance From Depreciation Regulation Of Price Cap LECs Is In The Public Interest And Will Promote Competition**

Forbearance from depreciation regulation of price cap LECs is consistent with the public interest, as required by section 10(a)(3) of the Communications Act. The requested forbearance will serve the public interest because the depreciation rules perform no useful purpose while placing substantial burdens on the price cap LECs and the Commission staff alike. Consistent with section 10(b) of the Communications Act, forbearance from depreciation regulation of price cap LECs will promote competitive market conditions. The requested forbearance will enhance competition in the provision of telecommunications services by improving the efficiency of the price cap LECs' operations and the Commission's own regulatory processes. Such promotion of competition will benefit consumers and justifies a positive public interest finding under section 10(a)(3).

As the Commission has focused on promoting telecommunications competition pursuant to the 1996 Act, its initiatives, coupled with growing competitive pressures, have heightened the need for price cap LECs to base their depreciation practices on market-derived economic factors, rather than regulations unrelated to the functioning of competitive markets. With forbearance in effect, price cap LECs will be able to recognize market-based economic depreciation factors, rather than regulatory prescriptions.<sup>41/</sup> Similarly, forbearance will serve the public interest by providing price cap LECs, like their competitors, the opportunity to recover their investments based on competitive market conditions rather than regulatory prescriptions. Thus, forbearance will enhance competition by eliminating obstacles to the price cap LECs' efficient operation in a manner similar to their competitors.<sup>42/</sup>

Continued depreciation regulation of the price cap LECs would disserve the public interest. With all incumbent LEC markets open to competition pursuant to the 1996 Act, the need for market-based depreciation practices is critical for those competitive markets to function successfully. As the Commission noted in eliminating the sharing mechanism for price cap LECs in 1997:

Interstate rate base and expense levels, and thus reported earnings, are also directly affected by accounting depreciation rates, which we prescribe for most incumbent price cap LECs. By contrast, in a competitive marketplace, decisions are governed by

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<sup>41/</sup> At the same time, as explained with respect to sections 10(a)(1) and (2) of the Communications Act, depreciation forbearance will not cause the price cap LECs' charges, practices, classifications, or regulations to be unjust or unreasonable, or unjustly or unreasonably discriminatory, and it will benefit, not harm, consumers.

<sup>42/</sup> As noted above, the requested forbearance will not affect state regulators' authority or ability to regulate the intrastate operations of the price cap LECs. States that use cost-of-service methods, including depreciation calculations, for intrastate regulation, retain the ability to evaluate depreciation rates independently.

economic costs and economic depreciation rates. Reduced reliance on accounting costs thus facilitates our transition to the competitive paradigm of the 1996 Act.<sup>43/</sup>

The additional step of forbearing from depreciation regulation of the price cap LECs is completely consistent with the competitive paradigm of the 1996 Act, and thus with the public interest. The elimination of sharing has laid the foundation for such forbearance.

As importantly, the public interest is best served when the Commission, the telecommunications industry, and consumers devote their valuable resources toward ensuring that the benefits of competition envisioned by the 1996 Act becomes reality. By forbearing from regulating the depreciation practices of the price cap LECs, the Commission will end for these carriers the history of costly, massive filings and contentious debates that have characterized the regulatory depreciation process through the years.<sup>44/</sup> In light of the detrimental effects of depreciation regulation on the competitive marketplace, forbearance would benefit the public interest by redeploying the resources of the Commission and the private sector that have been devoted to it.

#### IV. THE COMMISSION SHOULD MOVE SWIFTLY TO GRANT THE REQUESTED RELIEF

USTA requests the Commission to address this petition expeditiously, so that forbearance from depreciation regulation of price cap LECs can take effect on January 1, 1999. Rapid action will help consumers of the services provided by price cap LECs by promoting rational, market-based infrastructure development. When forbearance takes effect,

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<sup>43/</sup> Price Cap Order ¶ 152.

<sup>44/</sup> See *supra* page 6.

individual price cap LECs should not be precluded from making their cases to recover any depreciation reserve deficiencies that may exist. Consistent with the goals of the biennial review, early forbearance will also permit Commission resources to be deployed more effectively in the public interest.

## V. CONCLUSION

Forbearance from depreciation regulation of price cap LECs is required under the standards of section 10 of the Communications Act. Depreciation regulation is detrimental to consumers' interests, as well as the provision of efficient telecommunications services by price cap LECs in the competitive marketplace created by the 1996 Act. USTA requests the Commission to move rapidly to institute forbearance from such regulation by January 1, 1999.

Respectfully submitted,  
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September 21, 1998

## **CERTIFICATE OF SERVICE**

I, Mary-Helen Dove, hereby certify that on the 21st day of September, 1998, a true copy of the foregoing petition for forbearance of the United States Telephone Association was delivered to each of the following:

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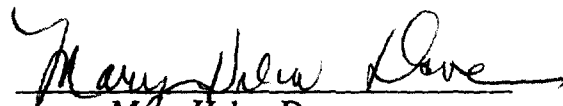
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